DEC 30 1999

Nos. 99-244 and 99-253

Supreme Court, U.S.
FILED
DEC 30 1999

In The

Supreme Court of the United States

No. 99-244

MOBIL OIL EXPLORATION & PRODUCING SOUTHEAST, INC.,

Petitioner,

v.

UNITED STATES,

Respondent.

and

No. 99-253

MARATHON OIL COMPANY,

Petitioner,

v.

UNITED STATES,

Respondent.

On Writs Of Certiorari To The United States Court Of Appeals For The Federal Circuit

BRIEF AMICUS CURIAE OF THE AMERICAN PETROLEUM INSTITUTE IN SUPPORT OF PETITIONERS

Of Counsel:

G. William Frick
David T. Deal
Douglas Morris
American Petroleum Institute
1220 L Street, Northwest
Washington, D.C. 20005-4070
(202) 682-8250

J. Berry St. John*
Craig Wyman
Liskow & Lewis
One Shell Square, 50th Floor
701 Poydras Street
New Orleans, LA 70139-5099
(504) 581-7979

Attorneys for American Petroleum Institute

**Counsel of Record*

December 30, 1999

27pp

TABLE OF CONTENTS

Page

TABLE OF CONTENTS i

TABLE OF AUTHORITIES ii

INTEREST OF AMICUS CURIAE 1

STATEMENT OF THE CASE 2

SUMMARY OF ARGUMENT 6

ARGUMENT 7

A. The Federal Circuit Decision Destroys the OCS Lease Bargain 7

1. The Decision Ignores the OCS Lease Terms by Focusing on "Permit Denials" 7

2. The Decision Fails to Enforce Reciprocal OCS Lease Performance 11

3. The Decision's Misguided View of Lease Performance Cannot Support Confiscation of the Lease Bonuses 13

4. The Decision Alters the OCSLA's Economic Risk Structure 16

B. The Integrity of the OCS Leasing Program is Vital to This Nation 19

CONCLUSION 23

TABLE OF AUTHORITIES

Page

CASES

United States v. National Exch. Bank, 270 U.S. 527 (1926) 6, 19

STATUTES AND REGULATIONS

Outer Continental Shelf Lands Act, 43 U.S.C. § 1331 *et seq*..... *passim*

Coastal Zone Management Act, 16 U.S.C. § 1451 *et seq*..... *passim*

Outer Banks Protection Act, Pub. L. No. 101-380, § 6003, 104 Stat. 484 (1990) 5

16 U.S.C. § 1456 ..... 5, 9

43 U.S.C. § 1332(3) 2, 19

43 U.S.C. § 1334 ..... *passim*

43 U.S.C. § 1337 3

43 U.S.C. § 1340 ..... *passim*

43 U.S.C. § 1351 ..... *passim*

GOVERNMENT PUBLICATIONS

Mineral Revenues 1998: Report on Receipts from Federal and Indian Leases, U.S. Department of the Interior, Minerals Management Service 20

MMS Offshore Stats, Third and Fourth Quarters 1998, U.S. Department of the Interior, Minerals Management Service 19, 21

MMS Revenue Collections, January-December 1998, U.S. Department of the Interior, Minerals Management Service 20, 21

TABLE OF AUTHORITIES – Continued

Page

Mineral Revenue Collections, January-September 1999, U.S. Department of the Interior, Minerals Management Service 20

1998 OCS Oil and Gas Production vs. Total U.S. Production; Safety, Leasing, Exploration, Production & Revenue Statistics; U.S. Department of the Interior, Minerals Management Service (June 1999), http://www.mms.gov/eod/stats.htm 19

Report to Congress on the Findings of the North Carolina Environmental Sciences Review Panel (April 6, 1992), Manuel Lujan, Secretary of the Interior 16

Statistical Highlights Fiscal Year 1997, U.S. Department of the Interior, Minerals Management Service (1998) 19

U.S. Bureau of Census, *Statistical Abstract of the United States: 1997* (117th Edition); Washington, D.C. (1997) 20

OTHER AUTHORITIES

Matthew Davis, STATE NEWS SERVICE (June 28, 1990) 15

21 Environment Reporter, *Current Developments*, p. 314 (BNA) June 8, 1990 14

Scott Pendleton, *Offshore Drilling Ban Draws Fire*, THE CHRISTIAN SCIENCE MONITOR, July 6, 1990 at 8 15

Patrick H. Martin, *Outer Continental Shelf Leases and Operating Regulations*, *in* 2 LAW OF FEDERAL OIL AND GAS LEASES, 25-1, 25-36 (Rocky Mtn. Min. L. Found. 1999) 4

INTEREST OF AMICUS CURIAE

Having followed quite closely this contract dispute between the United States and two private oil companies, Marathon Oil Company and Mobil Oil Exploration & Producing Southeast, Inc. ("Petitioners" or "Lessees"), the American Petroleum Institute ("API") once again finds it critically important to request an appearance and voice its concerns. Initially, API joined as amicus curiae in the Petitioners' rehearing request before the Federal Circuit below, after the first panel decision revealed a fatal miscomprehension of the Outer Continental Shelf Lands Act ("OCSLA"), through which the nation's offshore mineral leasing program is administered. While the Federal Circuit panel did grant a rehearing, its second decision contained only a superficial correction of the court's damage to ongoing Outer Continental Shelf ("OCS") lease activity. Believing that the law now established by the Federal Circuit decision, if left unmodified by this Court, would permanently harm this nation's OCS leasing program, API respectfully submits this amicus curiae brief in support of the Petitioners.[1]

API is a petroleum industry trade organization representing approximately 400 companies engaged in oil and gas exploration and production in the United States. The vast majority of the oil and gas leases on the OCS are held by API member companies, and API members have bid

---

[1] The parties have consented to the filing of this brief. Counsel for a party did not author this brief in whole or in part. No person or entity, other than the Amicus Curiae, its members, or its counsel made a monetary contribution to the preparation and submission of this brief.

tens of billions of dollars at OCS lease sales. In Amicus Curiae's view, the decision by the Federal Circuit has so misconstrued basic contractual law governing OCS lease operations that the OCS legal landscape has fundamentally shifted. The import of that decision's flawed contractual analysis will alter the economic risk structure of the OCSLA crafted by Congress after decades of experience and study. API is gravely concerned that this reallocation of economic risk will not only harm the oil and gas exploration and producing industry, but might actually threaten the viability of the entire OCS leasing program.[2] Amicus Curiae respectfully urges the Court to reverse the decision below.

STATEMENT OF THE CASE

The case is a breach of contract action brought against the United States relating to mineral leases issued to the Petitioners by the Minerals Management Service ("MMS") in an area of the Outer Continental Shelf offshore the State of North Carolina. While not disturbing the finding of the Court of Federal Claims that the government, through Congressional interference, had materially breached its leases with the Petitioners, the Federal Circuit decision voided the lower court's restitution award. The panel majority, with Judge Newman dissenting, found that objections to the Petitioners' lease

[2] The Congress has declared that the OCS is a *"vital national resource reserve . . .* which should be made available for expeditious and orderly development. . . . " 43 U.S.C. § 1332(3) (emphasis added).

exploration plans raised by the State of North Carolina under the Coastal Zone Management Act ("CZMA"), 16 U.S.C. § 1451, *et seq.*, essentially annulled all other concerns over the federal government's conduct. In so deciding, the court inflicted critical damage to the law governing OCS mineral leases that will have far-ranging and harmful effects on *all* holders of OCS leases. If the Federal Circuit's decision is allowed to stand, any future Congressional action thwarting an OCS lessee's existing contractual rights, if worked in tandem with state CZMA opposition, would authorize the federal government to confiscate the entirety of the lessee's investment in its lease – even if the federal government, as lessor, acknowledges that the lessee's exploration plans comply fully with all agency requirements. The damage to the OCS leasing program – the source of 25% of domestic natural gas production, and 22% of domestic oil production – could be severe.

The OCS mineral leases that are the subject of this dispute were issued by the MMS under the authority of the Outer Continental Shelf Lands Act, 43 U.S.C. § 1331 *et seq.* OCSLA leases require lessees to pay up-front cash bonuses, followed by periodic lease rental payments, for the tracts they acquire. 43 U.S.C. § 1337. Under the OCSLA statutory scheme, an OCS lessee may thereafter prepare a Plan of Exploration ("POE") as part of the "exploration" stage of lease activity.[3] If recoverable

[3] As described in a leading treatise on federal oil and gas law, the POE will include:

> a description of the type and sequence of exploratory activities; a description of drilling vessels, platforms,

resources are found, the lessee may then submit to the MMS a Plan of Development and Production, or "POD," to continue on to the "production" stage.[4] In the course of filing either plan, the OCSLA further stipulates that the OCS lessee will certify that its activities will be consistent with the coastal zone management plan of any affected state that has an approved CZMA program. *See* 43 U.S.C. § 1340(c)(2) (applying CZMA certification requirement to exploration plans); 43 U.S.C. § 1351(h) (applying the requirement to production plans).

For exploration plans, the OCSLA provides that the Secretary of the Interior, who acts through the MMS, "shall approve such plan . . . within thirty days of its submission, except that the Secretary shall disapprove

---

> and other structures to be used; the types of geophysical equipment that will be used; the location of each exploratory well planned; an oil spill contingency plan; an air-quality analysis; and other relevant geological and geophysical information. . . .
>
> If drilling affects a state with a federally-approved coastal zone management program, an Environmental Report (Exploration) must also be submitted. . . .

Patrick H. Martin, *Outer Continental Shelf Leases and Operating Regulations, in* 2 LAW OF FEDERAL OIL AND GAS LEASES, 25-1, 25-36 (Rocky Mtn. Min. L. Found. 1999).

[4] The POD "includes information similar to that in the exploration plan: the specific work to be performed; a description of drilling vessels, platforms, and pipelines together with safety and pollution control features and labor, material, and energy requirements; well locations; current interpretations of all relevant geological and geophysical data; environmental safeguards and safety standards; and a time schedule of the activities to undertaken." See Martin, *supra* at 25-38.

[the] plan" upon determining that (i) a proposed activity would result in a condition under 43 U.S.C. § 1334(a)(2)(A)(i) (which sets forth conditions for lease cancellation based on probable harm to life, property, or the environment), and (ii) the proposed activity cannot be modified to avoid such conditions. If the MMS disapproves an exploration plan for those specified reasons, the OCSLA expressly provides that the Secretary may cancel the lease and "the lessee shall be entitled to compensation. . . . " 43 U.S.C. § 1340(c)(1).

Finally, to aid this Court's appreciation of the background of this case, under 43 U.S.C. § 1351(h)(1)(B), the Secretary's initial approval of a POD includes a separate requirement, *not* applicable at the exploration stage, that the development and production plan either must have *already* received coastal zone consistency certification approval from any affected state, or the Secretary of Commerce must have already overridden the state's objection pursuant to 16 U.S.C. § 1456. If state CZMA approval or a Secretarial override cannot be shown in the first instance, 43 U.S.C. § 1351(h)(2)(A) carries the unique provision that the "lessee shall not be entitled to compensation [under the OCSLA] because of such disapproval [of the development and production plan]."

In the instant action, the Lessees prepared and filed a Plan of Exploration for their OCS leases pursuant to the OCSLA's exploration provisions, 43 U.S.C. § 1340. As expressly recognized by the Federal Circuit's decision, however, the MMS was prohibited from taking any action with regard to this POE by the Outer Banks Protection Act ("OBPA"), Pub. L. No. 101-380, § 6003, 104 Stat. 484, 555 (1990), enacted as a rider to the Oil Pollution Act of

1990, at the behest of the North Carolina delegation in Congress some nine years after issuance of the leases at issue.

SUMMARY OF ARGUMENT

The integrity of the leasing program established by the OCSLA, 43 U.S.C. § 1331 *et seq.*, is vital to this nation. The OCS program supplies an essential share of domestic energy production in addition to billions of dollars of non-tax governmental revenues. The grave and fundamental errors of hornbook contract law committed by the lower court in this OCS lease dispute have been soundly documented by the Petitioners. In reaching its result, the Federal Circuit decision has also devalued long-standing obligations of reciprocal contractual performance that make up the standard OCSLA lease agreement. Without doubt, the most disturbing aspect of the court's decision is the blanket denial of restitution or other compensation to an OCS lessee in the face of unilateral federal and state actions which thwart lease activity. Under the lower court's reasoning, every OCS lessee beginning lease exploration would now risk losing its entire lease investment – even if it complies fully with every MMS requirement. Amicus curiae respectfully requests this Court to correct these errors, to restore an OCS lessee's remedies of rescission and restitution, and to reaffirm the principle that "the United States does business on business terms." *United States v. National Exch. Bank*, 270 U.S. 527, 534 (1926).

ARGUMENT

A. The Federal Circuit Decision Destroys the OCS Lease Bargain.

1. The Decision Ignores the OCS Lease Terms by Focusing on "Permit Denials"

In describing the OCS Lessor/Lessee contractual relationship, the Federal Circuit decision on review recognized that the "[l]ease terms grant lessees the 'exclusive right and privilege to drill for, develop, and produce oil and gas resources' in exchange for an up-front cash bonus and periodic lease payments." See Mobil Petition Appendix ("Pet. App."), Docket No. 99-244 at 3a.[5] This statement captures the long-accepted understanding of the bargain struck by the parties to an OCS lease. In return for payments of up-front cash bonuses, followed by periodic lease rental payments, the lessee obtains the exclusive right, *if* its assessment of the leased property suggests further activity is warranted, to begin planning for the exploration and possible future development of the lease. Indeed, it was *at this very part of the lease process* – the filing of the POE – that the federal government's critical breach in this case – the eleventh-hour enactment of the OBPA – occurred.

The Federal Circuit's examination of the OCS lease relationship, however, stopped at this point. At first, the lower court seemed to recognize that the OBPA plainly interfered with existing contractual relationships: ("[t]o

[5] Citations to the decisions below will refer to the Pet. App. in Docket No. 99-244.

read the original contract between the parties as incorporating all future actions, whether by statute or regulation, by one of the parties would raise serious questions about illusory contracts, and perhaps questions of due process and other constitutional concerns.") Pet. App. 10a. But the panel majority then conducted a precipitous retreat: ("[i]n any event, because the outcome of the case does not turn on this issue, we need not further dwell upon it.") *Id.* Thereafter, avoiding any real focus on the impact of the OBPA on the government's contractual conduct, the panel majority locked its attention on a collateral issue involving an event subsequent to the POE filing, North Carolina's CZMA consistency objection.

The OBPA's enactment cannot be so lightly ignored. As correctly observed by the Court of Federal Claims, the OBPA *materially altered both the structure and framework of the Petitioners' leases, and the leasing process itself.* As such, the OBPA's new terms and conditions cannot be read into the Petitioners' leases. Moreover, as the court noted,

> common sense suggests that no sophisticated oil and gas company with many years of experience in drilling for oil in offshore leased tracts would knowingly agree to pay the huge, up-front considerations here involved for such tenuous and unilaterally interruptable drilling rights.

Pet. App. 63a.[6] This is a precise description of the nature of the government's breach in this case: the OBPA's "material alteration" of the structure and framework of the OCS lease bargain, and the attempted creation of

---

[6] *Conoco Inc. v. United States*, 35 Fed. Cl. 309, 324 (Fed. Cl. 1996).

"tenuous and unilaterally interruptable" drilling rights. Indeed, the crux of this dispute is the OBPA's effect of *wholesale contractual frustration.* It is *not,* as characterized by the Federal Circuit, a mere sideline dispute involving a "permit denial" or a CZMA "consistency complaint." Notwithstanding the Federal Circuit's re-characterization of this case as merely involving the filing of a single POE and a resultant "denial of permits," there *are no* actual "denials" of either a POE, or a permit application, in the record before this Court, because the OBPA prohibited MMS from even acting on the Lessees' POE.

The Federal Circuit panel's misguided discussion of "regulatory denials" was essentially the remainder of certain lines of reasoning that had underpinned the Federal Circuit panel's initial opinion, but were later removed. As noted earlier, the initial panel decision contained numerous errors in describing the interaction between the OCSLA and the CZMA and the proper construction of an OCS lessee's "performance." First, the initial panel decision had misread the OCSLA to require a lessee to receive CZMA state concurrence for its POE or face lease cancellation without compensation. The panel based its rejection of the restitution remedy on the Lessees' alleged resultant "violation" of the OCSLA.[7] But in

---

[7] Pet. App. 36a. (*Marathon Oil Co. v. U.S.*, 158 F.3d 1253 (Fed. Cir. 1998), superseded by *Marathon Oil Co. v. United States*, 177 F.3d 1331 (Fed. Cir. 1999)). The panel wrote that "[u]nder these circumstances, a lessee's options are to 'submit an amendment to such plan, or a new plan, to the Secretary of the Interior,' " *citing* 16 U.S.C. § 1456(c)(3)(B). Pet. App. 37a. But as amply demonstrated by Petitioners' arguments, the OBPA's serial delays would only have further frustrated their attempts to submit such an amended plan.

arriving at this conclusion, the court erroneously relied on 43 U.S.C. § 1351, the provision of the CZMA that applies to development and production plans, *not* plans of exploration. On rehearing, the panel corrected this error, by simply removing all direct references to § 1351.

In addition, the panel majority asserted that "North Carolina's legally valid objection to the consistency certification *left unfulfilled the requirement that the lessees demonstrate compliance with [all] applicable statutes and regulations.*" Pet. App. 12a. (Emphasis added.)[8] This statement finds no support in the CZMA, the OCSLA, or MMS regulations. The Lessees fully demonstrated "compliance with [all] applicable statutes and regulations," when adding the consistency certification, as called for by 43 U.S.C. § 1340(c)(2), to their POE filing. North Carolina's disagreement with that certification in no way establishes a failure by the Lessees to comply with the law.

The Federal Circuit decision under review now rests on a more narrowly-conceived legal analysis, *i.e.*, that North Carolina's CZMA consistency objection, per se,

---

[8] The original panel decision had gone even further, and reasoned that "under the circumstances of this case, to treat the *denial of the POE* as a breach of contract by the Government would be to eviscerate these salutary protections of the nation's fragile coastal lands and waters." App. 34a. (Emphasis added.) In other words, the panel had so misread the statute that it believed that the MMS was entitled to deny an exploration plan on CZMA consistency grounds. Instead, 43 U.S.C. § 1340, the section of the OCSLA dealing with exploration activity, *separates* the CZMA consistency certification approval process from the MMS's decision to approve or disapprove the plan of exploration. Once again, the panel's decision on rehearing dropped its reference to a POE "denial."

annulled all other concerns over the federal government's contractual conduct. The CZMA objection, by itself, has thus been elevated far beyond its tangential role in this OCS lease dispute.[9] As shown below, the panel's final decision not only refused to address the federal government's own OCS lease obligation, and thereby continued to misconstrue the law and the terms of the OCS lease, but also continued to ignore the federal government's own public record position on the effects of the OBPA, and on the Lessees' lease performance.

2. The Decision Fails to Enforce Reciprocal OCS Lease Performance

The Federal Circuit cited Section 10 of the MMS's OCS lease form, noting that it provides that lessees "shall comply with all regulations and orders relating to exploration, development, and production." Pet. App. 10a. Clearly, the lease carries with it attendant regulatory requirements, but as discussed in more detail below, the record shows that the MMS strongly endorsed the Petitioners' own lease compliance and performance in entering into the exploration stage of the leasing process. Moreover, as noted by the Court of Federal Claims:

> The lease agreements do not specifically state the parties' obligations regarding exploration plans but provide that the lessees agree to 'comply with all regulations and orders relating to

---

[9] To repeat: (1) there was no "denial" of the Lessees' POE by the MMS; and (2) there could have been no lawful denial of the Lessees' POE on CZMA consistency grounds.

> exploration.' Under the OCSLA and its regulations, exploration may only be conducted pursuant to approved exploration plans. Thus, in order to explore, plaintiffs are obligated to prepare and submit exploration plans. *The necessary reciprocal obligation is that the government will timely and fairly consider – not necessarily approve, but at least promptly consider – exploration plans properly submitted.*

Pet. App. 70a (emphasis added) (citing the MMS's express statutory duty under the OCSLA to approve or otherwise act on plans within thirty days of submission, 43 U.S.C. § 1340(c)(1)). Stated differently, "the contracts at issue provide that submission of plaintiffs' POEs is predicated on an *unequivocal governmental duty* to timely and fairly consider, though not necessarily approve, them." Pet. App. 72a (emphasis added). More tellingly, the Court of Federal Claims also recognized that:

> It is not necessary [to the finding of a contractual breach in this case] for plaintiffs to have actually submitted such exploration plans because it is clear [the United States] cannot and will not perform its end of the bargain as required by the OCSLA.

Pet. App. 73a. Thus, under the Court of Federal Claims' proper reading of Petitioners' OCS leases and the law of contracts, the Lessees are due restitution in this case even without consideration of their actual filing of a POE. *A fortiori*, the Lessees are entitled to restitution without consideration of an attendant POE filing event, *i.e.*, the lodging of North Carolina's CZMA objection.

3. The Decision's Misguided View of Lease Performance Cannot Support Confiscation of the Lease Bonuses

Avoiding analysis of the reciprocal obligations highlighted by the Court of Federal Claims, the Federal Circuit's decision instead attacked the Lessee's "performance." The panel majority repeatedly referred to the state's CZMA consistency objection to the POE, implying that such "environmental concerns" excuse or even validate the government's contractual misconduct. For example, the panel majority wrote that "North Carolina's legally valid objection to the consistency certification left unfulfilled the requirement that the lessees demonstrate compliance with applicable statutes and regulations, compliance with which was a prerequisite to obtaining the necessary permits and licenses." Pet. App. 12a. Two paragraphs later, the court starkly suggests that any finding of federal misconduct in the role played by the OBPA in Petitioners' lease delays would be tantamount to "eviscerat[ing] . . . salutary protections of the nation's fragile coastal lands and waters." Pet. App. 13a. These observations lack foundation.

The Federal Circuit's complaint of Petitioners' "nonperformance" completely ignored the fact that the MMS has repeatedly described the "lease performance" on the record in superlative terms. For example, the MMS Deputy Director characterized the 2,000 page Environmental Report prepared for the Lessees' Manteo project as "the most comprehensive body of environmental information

ever assembled on a proposed well in the history of the U.S. offshore drilling program."[10]

Moreover, at the time of its filing the MMS announced that the Petitioners' POE was the *most comprehensive exploration plan ever submitted to the agency*.[11] Finally, Interior Secretary Lujan publicly acknowledged that the Lessees' POE, as submitted, was "approvable in all respects" under all MMS requirements, and that the agency's hands were tied by the provisions of the OBPA – *not* by agency concerns over the "salutary protections of the Nation's fragile coastal lands and waters."[12] In other words, the government, as lessor, never asserted that the Lessees' project

---

[10] 21 Environment Reporter, *Current Developments*, (BNA) June 8, 1990, p. 314; *see also* Fed. Cir. J.A. 949-50.

[11] September 29, 1990 MMS News Release. The MMS even submitted public comments strongly supporting the Lessees' request to the Secretary of Commerce to override North Carolina's CZMA objections. In these public comments, the MMS observed that:

> An unbiased consideration of the analyses and conclusions contained within the Final [Environmental Report] and the [Environmental Assessment] will result in a determination that no significant effects are expected in the area of the Manteo Prospect, or to the State's coastal zone resources, as a result of Mobil drilling a single exploration well nearly *39 miles* from shore.

MMS Comments, June 4, 1991 at p. 9 (emphasis in original).

[12] Pet. App. 13a; Fed. Cir. J.A. 963. Moreover, Amicus Curiae would note that, as the legislative history of the OBPA cited by Petitioners clearly reveals, North Carolina's CZMA "consistency objection" was merely a single weapon in a formidable political arsenal to oppose drilling off its coastline without regard to particular environmental impacts. Indeed, months before the State's consistency objection based on

raised serious "environmental concerns," and the Federal Circuit inappropriately introduced this issue into the lease dispute.

Moreover, the Federal Circuit found that the effect of the OBPA on Petitioners' leases was of no moment, because "appellees' failure to overcome North Carolina's objections resulted in a delay that preceded and extended throughout the period in which the OBPA was effective." Pet. App. 13a. This assertion is directly undercut by the federal government's own actions. The *MMS*, recognizing the dictates of the OBPA, issued *sua sponte* in 1990 a unilateral suspension of ongoing operations for the Petitioners' North Carolina leases based solely on the OBPA. Moreover, Interior Secretary Lujan stated publicly that the OBPA would require additional delays, and the preparation of additional studies, far into the development

---

"insufficient information" *was even issued*, the public record confirms that North Carolina Governor James G. Martin had already announced, in correspondence to President Bush, that North Carolina was opposed to offshore drilling before the year 2000, regardless of the completion of any "new studies," or, for that matter, any showing of the absence of adverse impacts of Petitioners' exploratory drilling activity. See Scott Pendleton, *Offshore Drilling Ban Draws Fire*, THE CHRISTIAN SCIENCE MONITOR, July 6, 1990 at 8, *available in* LEXIS, News Library, Arcnews File (reporting Governor Martin's correspondence to the President, and his corresponding entreaty for help from the State's congressional delegation); Matthew Davis, STATE NEWS SERVICE, June 28, 1990 *available in* LEXIS, News Library, Arcnews File (describing the "solid front" formed by Governor Martin and the North Carolina congressional delegation to oppose offshore drilling).

and production stage of Lessee's OCS leases: "The objectives of any future . . . recommended studies will be reviewed at each phase of development."[13]

4. The Decision Alters the OCSLA's Economic Risk Structure

Even while acknowledging that the OBPA and subsequent events may have affected the Petitioners' rights to explore and develop their OCS tracts, the Federal Circuit nevertheless authorized the confiscation of Petitioners' up-front "bonuses," asserting that it could find

> no principled distinction between a lessee whose hopes for large rewards from such a lease are frustrated by a failure to obtain the necessary permits for exploration, and those of a lessee whose hopes are drowned by impossible weather, equipment failures, financial setbacks, or any number of other circumstances beyond the lessee's control. In either case, the lessee contracted for the exclusive opportunity to explore in a certain area; the inability of a lessee to explore, if not attributable to the Government, does not create an entitlement to any refund of the consideration paid to obtain the lease.

Pet. App. 15a. Thus, the court saw no "principled distinction" between *force majeure* or other accidental events, and the Congress's imposition, at the instance of the

---

[13] *Report to Congress on the Findings of the North Carolina Environmental Sciences Review Panel* (April 6, 1992), Manuel Lujan, Secretary of the Interior, Fed. Cir. J.A. 414.

North Carolina delegation, of the political gauntlet of the OBPA.

In its ruling, the Federal Circuit's majority decision overturned a long-standing and vital principle underlying the essential OCS lease bargain: the OCS lessee's "huge, up-front considerations" are payment for the essential right to explore for oil and gas which *may or may not* be found. Restated, the reward of successfully finding and profitably producing oil and gas is balanced against the overarching risk, borne by the OCS lessee, that the oil and gas will *not* be found, or cannot be produced in profitable quantities. That risk includes the OCS lessee's exposure of not only the loss of its upfront bonus payments, but often the loss of additional substantial investments, involving many millions of dollars, devoted to initial lease exploration and development activity. Now, the Federal Circuit would expand the lessee's risk even further – finding a facile analogy between the risk of dilatory *force majeure* events or other contingencies, and the OBPA's serial array of governmental obstacles that completely stifled Petitioners' lease activities – and thereby toppling the bargain between OCS lessees and the government. In fact, as duly noted by the Petitioners, the Federal Circuit's decision casts into doubt a basic contractual balance underlying not only the thousands of currently outstanding OCS leases, but also an untold number of other highly valuable government contracts.

Judge Newman's dissent captures the essence of the Federal Circuit's error. When encountering the same passage from the majority opinion quoted above, Judge Newman recognized that

> [such an] analysis is not supportable by any legal or equitable theory. What [Petitioners] paid for was the right of exploration. [Petitioners] bore the risk that the exploration might fail to find oil or gas, but [Petitioners] did not bear the risk that exploration would be entirely barred, especially by the same party from whom it bought the right.

Pet. App. 21a. In Judge Newman's view, this case posed this fundamental question: "whether the government shall deal fairly and legally with its contracting partners." Pet. App. 18a. Casting the answer in the affirmative, Judge Newman recognized that the effect of OBPA, enacted in the midst of the CZMA consistency process for the drilling of an initial exploratory well, *"does not justify the federal government's confiscation of [Petitioners'] payment[s] for a contract entered into before any such objection[s] arose." Id.* (Emphasis added.)

This Court should correct the Federal Circuit's grave error in order to preserve the integrity of the OCS leasing program. If the panel's ruling is left in place, OCS lessees will be subject to a rule that allows the government to confiscate their entire lease consideration if a newly-enacted federal statute arbitrarily upsets both ongoing and future lease operations, which the CZMA consistency certification process also frustrates. If allowed to stand, this erroneous ruling would rearrange the entire economic structure of the OCSLA, thereby shifting enormous and unintended economic risks to lessees. And, as ably observed by the Petitioners, the Federal Circuit's decision creates an even larger uncertainty as to when the remedies of rescission and restitution are *ever* available against the federal government – effectively vitiating the

fundamental presumption underlying government contracting that "[t]he United States does business on business terms." *United States v. National Exch. Bank*, 270 U.S. 527, 534 (1926).

B. The Integrity of the OCS Leasing Program is Vital to This Nation

The widespread effects of the Federal Circuit decision on other OCS lessees and on the future of the OCS leasing program should lead the Court to reverse the Federal Circuit decision. The OCS leasing program is vital to the nation.[14] By the end of 1998, over eleven billion barrels of oil and 130 trillion cubic feet of natural gas have been produced under the OCS leasing program.[15] In 1998, the OCS accounted for fully 25% of domestic natural gas production and 22% of domestic oil production.[16]

At the end of 1998, nearly 8,300 oil and gas leases issued under the OCSLA existed on the nation's Outer

---

[14] The Congress has declared that the OCS is a *"vital national resource reserve* . . . which should be made available for expeditious and orderly development. . . . " 43 U.S.C. § 1332(3) (emphasis added).

[15] *Statistical Highlights Fiscal Year 1997*, U.S. Department of the Interior, Minerals Management Service (1998); *MMS Offshore Stats, Third and Fourth Quarters 1998*, U.S. Department of the Interior, Minerals Management Service.

[16] *1998 OCS Oil and Gas Production v. Total U.S. Production; Safety, Leasing, Exploration, Production & Revenue Statistics;* U.S. Department of the Interior, Minerals Management Service (June 1999), http://www.mms.gov/eod/stats.htm.

Continental Shelf.[17] Additional leases have been issued by the MMS in 1999, and lease sales will continue into the foreseeable future. Over the last ten and one-half years alone, OCS lessees have paid the federal government over $6 billion in lease bonuses.[18] Indeed, the MMS collected over $1.4 billion in lease bonuses in 1997, and another $1.3 billion in 1998.[19] As of September of this year, over 84% of all oil royalties paid on Federal and Indian leased lands, and over 77% of gas royalties, came from the OCS.[20]

If the Federal Circuit's ruling is allowed to stand, all OCS lessees, as well as bidders at future OCS lease sales, will be faced with stark uncertainties regarding the OCSLA statutory scheme. The most disturbing aspect of the court's decision is the denial of restitution or other compensation to a lessee in the face of unilateral federal

---

[17] *Mineral Revenues 1998, Report on Receipts From Federal and Indian Leases*, U.S. Department of the Interior, Minerals Management Service. The number of offshore leases rose 12.5% in 1998, from 7,359 leases in 1997. *Id.*

[18] U.S. Bureau of Census, *Statistical Abstract of the United States: 1997* (117th Edition); Washington, D.C. (1997); *MMS Revenue Collections, January-December 1998*, U.S. Department of the Interior, Minerals Management Service; *MMS Revenue Collections, January-September 1999*, U.S. Department of the Interior, Minerals Management Service.

[19] *Mineral Revenue Collections, January-December 1998, supra* n.18. Bonuses received in the first three quarters of 1999 totaled $159 million. *MMS Revenue Collections, January-September 1999, supra* n.18.

[20] *Mineral Revenue Collections, January-September 1999, supra* n.18.

and state actions thwarting lease activity. Under this reasoning, every OCS lessee beginning lease exploration would now risk losing its entire lease investment – even if it complies fully with every MMS requirement. As observed by the Court of Federal Claims, "common sense suggests that no sophisticated oil and gas company with many years of experience in drilling for oil in offshore leased tracts would knowingly agree to pay the huge, up-front considerations . . . for such tenuous and unilaterally interruptable drilling rights." Pet. App. 63a.

MMS lease records lend perspective to that court's observation: As of the end of 1998, only about 20% of existing OCS leases were in the "production" stage, meaning that wells had been drilled on those leases that were producing oil or natural gas.[21] Thus, the vast majority of existing leases issued under the OCSLA are still in (or again facing) the "exploration" stage of lease activity.[22] Considering that virtually all of these active leases are located offshore of states with approved coastal zone management programs, each and every one of these OCS lessees which pursues exploration will undergo the CZMA consistency certification process as part of its OCS

---

[21] *Mineral Revenues 1998, supra* n.17.

[22] Between 1988 and 1998, nearly 4,100 exploratory wells were drilled on over 43,000,000 acres under lease on the OCS. *Mineral Revenues 1998, supra* n.17; *MMS Offshore Stats, Third & Fourth Quarters 1998, supra* n.15. Some OCS leases that are not currently "producing" could contain now-depleted wells, thus rendering those leases also subject to a return to the exploration stage of activity.

drilling plans.[23] Therefore, the import of the Federal Circuit's decision, which has shattered protections afforded to lessees that must use that process, has potential impacts on countless present, and future, lease planning efforts.

API is also concerned that the Federal Circuit's implicit endorsement of North Carolina's objection to the POE consistency certification due to the "inadequacy of information" will only embolden other coastal states that philosophically oppose offshore development to misuse the CZMA and OCSLA processes. In addition, the reasoning of the court's decision can only encourage other Congressional interference with OCS mineral exploration and development activity for overtly political reasons. Under the lower court's ultimate ruling, if such future Congressional action is accompanied by contemporaneous state CZMA objections, the government may breach its leases with impunity. Accordingly, the industry's incentive to bid for OCS leases, especially in new, frontier OCS areas, will be drastically undercut.

---

[23] *See* 43 U.S.C. § 1340(c)(2) (applying CZMA consistency certification requirements to exploration plans); *cf.* 43 U.S.C. § 1351.

CONCLUSION

For the reasons stated above, the Court should reverse the Federal Circuit decision.

Respectfully submitted,

Of Counsel:

G. William Frick
David T. Deal
Douglas Morris
American Petroleum Institute
1220 L Street, Northwest
Washington, D.C. 20005-4070
(202) 682-8250

J. Berry St. John*
Craig Wyman
Liskow & Lewis
One Shell Square, 50th Floor
701 Poydras Street
New Orleans, LA 70139-5099
(504) 581-7979

Attorneys for American Petroleum Institute

**Counsel of Record*